HON'BLE THE CHIEF JUSTICE SRI G.S. SINGHVI

AND

HON'BLE SRI JUSTICE G.V. SEETHAPATHY

Writ Petition No.11471 of 2006

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Between:

Rayalaseema Jute Mills Ltd.,

rep. by its Managing Director,

T. Sridhar Gupta

… Petitioner

And

Deputy General Manager,

Industrial Development Bank of India Ltd.,

Chennai and another.

… Respondents

:: ORDER ::

Counsel for the petitioner: Sri D. Vijaya Chandra Reddy

Dated: 13th June, 2006

Per G.S.Singhvi, C.J.

The Recovery of Debts due to Banks and Financial Institutions Act, 1993 (for short 'the 1993 Act') was enacted by the Parliament in the backdrop of pendency of large number of civil suits filed by the banks and other financial institutions for recovery of public money. The tardy process of the civil courts and dilatory tactics adopted by the defaulters resulted in a virtual deadlock and consequential frustration of the attempt of the banks and financial institutions to recover their dues. It was thought that with the establishment of special adjudicatory bodies i.e., Debts Recovery Tribunals, situation will improve and the recovery of monies due to banks and financial institutions would be expedited. In first few years, the tribunals established under Section 3 of the 1993 Act proved their worth and some progress was made in the right direction, but with the passage of time, the proceedings of the tribunals became akin to those of civil courts. By 2001, a sum of Rs.1,20,000/- crores belonging to the banks and public financial institutions was said to be due. This compelled the government to bring new legislation i.e., Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (for short 'the 2002 Act') for recovery of dues of the banks etc. The provisions of the 2002 Act are far more stringent and non-obstante clause contained in Section 35 gives overriding effect to the provisions of the new Act qua all other laws including the 1993 Act. The constitutionality of the 2002 Act was challenged in various High Courts and the Supreme Court. I n **Mardia Chemicals v. Union of India**, the Supreme Court considered various facets of challenge and negatived the same except Section 17 (un-amended) which envisaged deposit of 75 per cent of the dues as a condition precedent to the entertaining of appeal. Paras 34 to 36 of that judgment which contain the backdrop of the 2002 Act and the Supreme Court's disinclination to entertain challenge to its constitutionality read as under:

> " Some facts which need to be taken note of are that the banks and the financial institutions have heavily financed the petitioners and other industries. It is also a fact that a large sum of amount remains unrecovered. Normal process of recovery of debts through courts is lengthy and time taken is not suited for recovery of such dues. For

financial assistance rendered to the industries by the financial institutions, financial liquidity is essential failing which there is a blockade of large sums of amounts creating circumstances which retard the economic progress followed by a large number of other consequential ill effects. Considering all these circumstances, the Recovery of Debts Due to Banks and Financial Institutions Act was enacted in 1993 but as the figures show it also did not bring the desired results. Though it is submitted on behalf of the petitioners that it so happened due to inaction on the part of the Governments in creating Debts Recovery Tribunals and appointing presiding officers, for a long time. Even after leaving that margin, it is to be noted that things in the spheres concerned are desired to move faster. In the present-day global economy it may be difficult to stick to old and conventional methods of financing and recovery of dues.

Hence, in our view, it cannot be said that a step taken towards securitisation of the debts and to evolve means for faster recovery of NPAs was not called for or that it was superimposition of undesired law since one legislation was already operating in the field, namely, the Recovery of Debts Due to Banks and Financial Institutions Act. It is also to be noted that the idea has not erupted abruptly to resort to such a legislation. It appears that a thought was given to the problems and the Narasimham Committee was constituted which recommended for such a legislation keeping in view the changing times and economic situation whereafter yet another Expert Committee was constituted, then alone the impugned law was enacted. Liquidity of finances and flow of money is essential for any healthy and growth-oriented economy. But certainly, what must be kept in mind is that the law should not be in derogation of the rights which are guaranteed to the people under the Constitution. The procedure should also be fair, reasonable and valid, though it may vary looking to the different situations needed to be tackled and object sought to be achieved.

As referred to above, the Narasimham Committee was constituted in 1991 relating to the financial system prevailing in the country. It considered wide-ranging issues relevant to the economy, banking and financing, etc. Under Chapter V of the Report under the heading “Capital Adequacy, Accounting Policies and other Related Matters”, it was opined that a proper system of income recognition and provisioning is fundamental to the preservation of the strength and stability of the banking system. It was also observed that the assets are required to be classified, it also takes note of the fact that Reserve Bank of India had classified the advances of a bank, one category of which was bad debts/doubtful debts. It then mentions that according to the international practice, an asset is treated as non-performing when the interest is overdue for at least two quarters. Income of interest is

considered as such, only when it is received and not on the accrual basis. The Committee suggested that the same should be followed by the banks and financial institutions in India and an advance is to be shown as non-performing assets where the interest remains due for more than 180 days.

It was further suggested that Reserve Bank of India should prescribe clear and objective definitions in respect of advances which may have to be treated as doubtful, standard or substandard, depending upon different situations. Apart from recommending the setting up of Special Tribunals to deal with the recovery of dues of the advances made by the banks, the Committee observed that impact of such steps would be felt by the banks only over a period of time, in the meanwhile, the Committee also suggested for reconstruction of assets saying:

"The Committee has looked at the mechanism employed under similar circumstances in certain other countries and recommends the setting up of, if necessary by special legislation, a separate institution by the Government of India to be known as 'Assets Reconstruction Fund' (ARF) with the express purpose of taking over such assets from banks and financial institutions and subsequently following up on the recovery of dues owed to them from the primary borrowers."

While recommending for setting up of Special Tribunals, the Committee observed:

"Banks and financial institutions at present face considerable difficulties in recovery of dues from the clients and enforcement of security charged to them due to the delay in the legal processes. A significant portion of the funds of banks and financial institutions is thus blocked in unproductive assets, the values of which keep deteriorating with the passage of time. Banks also incur substantial amounts of expenditure by way of legal charges which add to their overheads. The question of speeding up the process of recovery was examined in great detail by a Committee set up by the Government under the Chairmanship of the late Shri Tiwari. The Tiwari Committee recommended, inter alia, the setting up of Special Tribunals which could expedite the recovery process…."

The Committee also suggested some legislative measures to meet the situation.

In its Second Report, the Narasimham Committee observed that NPAs in 1992 were uncomfortably high for most of the public sector banks. In Chapter VIII of the Second Report the Narasimham

Committee deals about legal and legislative framework and observed:

> "*8.1.* A legal framework that clearly defines the rights and liabilities of parties to contracts and provides for speedy resolution of disputes is a sine qua non for efficient trade and commerce, especially for financial intermediation. In our system, the evolution of the legal framework has not kept pace with changing commercial practice and with the financial sector reforms. As a result, the economy has not been able to reap the full benefits of the reforms process. As an illustration, we could look at the scheme of mortgage in the Transfer of Property Act, which is critical to the work of financial intermediaries...."

One of the measures recommended in the circumstances was to vest the financial institutions through special statutes, the power of sale of the assets without intervention of the court and for reconstruction of assets. It is thus to be seen that the question of non-recoverable or delayed recovery of debts advanced by the banks or financial institutions has been attracting attention and the matter was considered in depth by the Committees specially constituted consisting of the experts in the field. In the prevalent situation where the amounts of dues are huge and hope of early recovery is less, it cannot be said that a more effective legislation for the purpose was uncalled for or that it could not be resorted to. It is again to be noted that after the Report of the Narasimham Committee, yet another Committee was constituted headed by Mr Andhyarujina for bringing about the needed steps within the legal framework. We are therefore, unable to find much substance in the submission made on behalf of the petitioners that while the Recovery of Debts Due to Banks and Financial Institutions Act was in operation it was uncalled for to have yet another legislation for the recovery of the mounting dues. Considering the totality of circumstances and the financial climate world over, if it was thought as a matter of policy to have yet speedier legal method to recover the dues, such a policy decision cannot be faulted with nor is it a matter to be gone into by the courts to test the legitimacy of such a measure relating to financial policy."

In paragraphs 45 and 46, the Supreme Court adverted to the remedies available to the persons aggrieved by proceedings initiated under the 2002 Act and observed:

"In the background we have indicated above, we may consider as to what forums or remedies are available to the borrower to ventilate his grievance. The purpose of serving a notice upon the borrower under sub-section (2) of Section 13 of the Act is, that a reply may be submitted by the borrower explaining the reasons as to why measures may or may not be taken under sub-section (4) of Section 13 in case of non-compliance with notice within 60 days. The creditor must apply its mind to the objections raised in reply to such notice and an internal mechanism must be particularly evolved to consider such objections raised in the reply to the notice. There may be some meaningful consideration of the objections raised rather than to ritually reject them and proceed to take drastic measures under sub-section (4) of Section 13 of the Act. Once such a duty is envisaged on the part of the creditor it would only be conducive to the principles of fairness on the part of the banks and financial institutions in dealing with their borrowers to apprise them of the reason for not accepting the objections or points raised in reply to the notice served upon them before proceeding to take measures under sub-section (4) of Section 13. Such reasons, overruling the objections of the borrower, must also be communicated to the borrower by the secured creditor. It will only be in fulfilment of a requirement of reasonableness and fairness in the dealings of institutional financing which is so important from the point of view of the economy of the country and would serve the purpose in the growth of a healthy economy. It would certainly provide guidance to the secured debtors in general in conducting the affairs in a manner that they may not be found defaulting and being made liable for the unsavoury steps contained under sub-section (4) of Section 13. At the same time, more importantly, we must make it clear unequivocally that communication of the reasons for not accepting the objections taken by the secured borrower may not be taken to give occasion to resort to such proceedings which are not permissible under the provisions of the Act. But communication of reasons not to accept the objections of the borrower, would certainly be for the purpose of his knowledge which would be a step forward towards his right to know as to why his objections have not been accepted by the secured creditor who intends to resort to harsh steps of taking over the management/business of viz. secured assets without intervention of the court. Such a person in respect of whom steps under Section 13(4) of the Act are likely to be taken cannot be denied the right to know the reason of non-acceptance and of his objections. It is true, as per the provisions under the Act, he may not be entitled to challenge the reasons communicated or the likely action of the secured creditor at that point of time unless his right to approach the Debts Recovery Tribunal as provided under Section 17 of the Act matures on any measure having been taken under sub-section (4) of Section 13 of the Act.

We are holding that it is necessary to communicate the reasons for not accepting the objections raised by the borrower in reply to the notice under Section 13(2) of the Act, more particularly for the reason that normally in the event of non-compliance with notice, the party giving notice approaches the court to seek redressal but in the present case, in view of Section 13(1) of the Act the creditor is empowered to enforce the security himself without intervention of the court. Therefore, it goes with logic and reason that he may be checked to communicate the reason for not accepting the objections, if raised and before he takes the measures like taking over possession of the secured assets, etc."

In Writ Petition Nos. 26663 and 27553 of 2006 (**M/s Sidhhi Vinayaka Hotels (P) Ltd., v. The Union of India**), decided on February 17, 2006, a Division Bench of this Court of which one of us was a member, considered and negated challenge to Section 14 of the 2002 Act. Some of the observations made in that judgment are also reproduced below:

"An analysis of the above reproduced provisions show that by virtue of non-obstante clause contained in sub-section (1) of section 13 any security interest created in favour of any secured creditor may be enforced without the intervention of the court or tribunal. In terms of sub-section (2) the secured creditor can issue notice to the borrower requiring the latter to discharge his liabilities within sixty days from the date of notice. Such notice is required to be delivered in accordance with Rule 3 of the Rules. On receipt of notice issued under sub-section (2), the borrower can make a representation or raise objection against the demand. The secured creditor is required to consider such representation or objection. If it is found that the representation or objection is not acceptable or tenable, then the secured creditor is duty bound to communicate the reasons for non-acceptance to the borrower. If the borrower fails to discharge his liability in full within a period of sixty days specified in sub-section (2), the secured creditor can take recourse to one or the other mode as specified in sub-section (4). One of the modes is to take over the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realizing the secured asset. The secured creditor can also appoint any person to manage the secured assets of which possession has been taken over. Any person who may have acquired any of the secured assets from the borrower can also be called upon to

pay such sum of money as may be sufficient to pay the secured debt. Section 14 (1) lays down that where the possession of any secured asset is required to be taken by the secured creditor or if any of the secured asset is required to be sold or transferred by the secured creditor, then he may, for the purpose of taking possession or control of any such secured asset make an application in writing to the Chief Metropolitan Magistrate or the District Magistrate within whose jurisdiction any such secured asset or other documents relating thereto is situated or is found for taking possession thereof. On receipt of such request, the Chief Metropolitan Magistrate or as the case may be, the District Magistrate shall take possession of the asset or document and forward the same to the secured creditor. Sub-section (2) of Section 14 empowers the Chief Metropolitan Magistrate or the District Magistrate to take appropriate steps or use, or cause to be used, such force, as may be necessary for taking possession of secured assets and documents relating thereto. Sub-section (3) of Section 14 declares that any action taken by the Chief Metropolitan Magistrate or the District Magistrate under Section 14 shall not be called in question by any court or before any authority. Section 17 which is captioned as “Right to appeal” lays down that any person (including the borrower) aggrieved by any of the measures taken under sub-section (4) of Section 13 by the secured creditor or his authorized officer can make an application to the Debts Recovery Tribunal within forty five days from the date of taking of such measures. Under sub-section (2) of Section 17 the Debts Recovery Tribunal is required to consider whether any of the measures taken by the secured creditor under sub-section (4) of Section 13 for enforcement of security is in accordance with the provisions of the Act and Rules made there under. If the Tribunal comes to the conclusion that such measure is not in accordance with the provisions of the Securitisation Act and the Rules, then it may require restoration of management of business to the borrower or restoration of possession of the secured assets and declare that the action taken by the secured creditor is invalid. The Tribunal can pass any other appropriate order in regard to the steps taken by the secured creditor under Section 13 (4). If the Tribunal declares that the action taken by the secured creditor is in consonance with sub-section (4) of Section 13 then such creditor can take recourse to one or more of the modes mentioned in Section 13 for the purpose of recovery of secured debts.

A conjoint reading of Section 13 (4) and 14 makes it clear that the source of power to take possession of the secured assets of the borrower can be traced in Section 13 (4) and not under Section 14, which has been enacted as an aid for execution of the decision taken by the secured creditors to take possession of the secured assets or documents. To put it differently the substantive provision entitling the secured creditor to take possession of the secured assets is contained

in Section 13 (4) and Section 14 merely contains a provision to facilitate taking over of possession without any impediment. If a person feels aggrieved by the action of the secured creditor to take possession of the secured asset, then he can file an application under Section 17 (1) before the Tribunal and the Tribunal can, after examining the facts and circumstances of the case and evidence produced by the parties declare that the action taken by the secured creditor is not inconsonance with Section 13 (4). The Tribunal can also direct the secured creditor to restore the possession of the secured assets of the borrower.

In view of the above analysis of the relevant provisions, we are inclined to agree with Shri Mohan Parasaran that right of appeal/representation available to the aggrieved person under Section 17 can be exercised as and when the secured creditor decides to take possession of the property. He can also challenge order passed by the Chief Judicial Magistrate or the District Magistrate, as the case may be, under section 14 of the Securitisation Act.

If Section 14 is read in the manner indicated above, it is not possible to accept the argument of the learned counsel for the petitioners that the same is violative of Article 14 of the Constitution.

We have prefaced disposal of this petition by making reference to the judgments of the Supreme Court in **Mardia Chemicals v. Union of India** (supra) and of this Court in **Siddhi Vinayaka Hotels (P) Ltd., v. Union of India** (supra), because after perusing the averments contained in the affidavit filed in support of this petition and hearing Sri D.Vijaya Chandra Reddy, learned counsel for the petitioner, we are convinced that there is no merit in the petitioner's challenge to notices dated 12-1-2006 and 3-5-2006 issued by Industrial Development Bank of India Limited (for short, 'the bank') for recovery of Rs.4,49,57, 683/-.

The petitioner is a company registered under the Companies Act, 1956. It is engaged in manufacture of jute threads. In 1989, the petitioner took term loan of Rs.170 lacs from the bank. On account of petitioner's failure to repay the loan, the bank filed an application under Section 19 of the 1993 Act. During the pendency of that application, the bank issued notice dated 12-1-2006 under Section 13 (2) of the 2002 Act requiring the petitioner to pay Rs.4,49,57,683/- with a stipulation that if the amount is not paid, action will be taken under Part III of the 2002 Act. The petitioner sent reply dated 7-4-2006 stating therein that the application filed by the Bank under

Section 19 of the 1993 Act is pending before the Debts Recovery Tribunal at Hyderabad. This was followed by notice dated 3-5-2006 vide which the bank again called upon the petitioner to repay the amount due.

The petitioner has challenged the aforementioned two notices by contending that without withdrawing the application filed under Section 19 of the 1993 Act, the bank could not have resorted to Section 13 of the Act for recovery of its dues.

Sri D.Vijaya Chandra Reddy made strenuous efforts to persuade us to nullify the impugned notices by arguing that without withdrawing the application filed under Section 19 of the Act, as amended in 2004, the bank could not have resorted to stringent measures envisaged under Sections 13 (2) and 13 (4) of the 2002 Act. Learned counsel invoked the doctrine of election and submitted that the bank cannot pursue two parallel proceedings with the avowed object of recovery of its dues.

We have considered the submissions of the learned counsel, but have not felt persuaded to agree with him. In our opinion, the non-obstante clause contained in Section 35 of the 2002 Act gives overriding effect to that Act qua the provisions of the 1993 Act. Therefore, pendency of an application filed under Section 19 of the 1993 Act cannot be treated as a bar to the invoking of provisions contained in Chapter III of the 2002 Act. Amended Section 19 of the 1993 Act merely enables the bank to file an application before the tribunal for withdrawal of the proceedings. However, omission on the bank's part to file such an application does not operate as an impediment to the initiation of proceedings under Section 13 of the 2002 Act and the notices impugned in this petition cannot be nullified only on the ground that the Bank did not move the Tribunal for withdrawal of the application.

There is another reason for our disinclination to entertain the writ petition i.e. the petitioner's failure to avail the remedies available to it under Section 13 (3A) and 17 of the 2002 Act. Section 13 (3A) contemplates filing of objections by the person to whom notices issued by the secured creditor. It also imposes a duty on the secured creditor to consider the objections and decide the same. If an action is taken under Section 13 (4), the noticee can avail remedy by filing an application under Section 17 of the 2002 Act. These remedies must be treated as effective alternative

remedies in view of the judgment of the Supreme Court in **Mardia Chemicals v. Union of India** (supra) and of this Court in **Siddhi Vinayaka Hotels (P) Ltd. v. The Union of India** (supra).

For the reasons mentioned above, the writ petition is dismissed.

G.S.SINGHVI, C.J.

13th June, 2006

G.V.SEETHAPATHY, J.

ARS/GRR/svs